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FINANCIAL INNOVATION AND DONOR INTERVENTION IN AFRICA: THE VILLAGE SAVINGS AND CREDIT ASSOCIATIONS (VISACAs) IN THE GAMBIA.

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Abstract

This paper documents the unusual performance of the Village Savings and Credit Association (VISACAs) in The Gambia. Important organizational and operational technologies are highlighted in successfully supplying a range of financial services to their members. The important issue of the appropriate type of donor intervention is also explored.

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Formal and informal financial markets in The Gambia are made up of many segments. Banks, village savings and credit associations, cooperatives, non-governmental organizations, private traders, suppliers and microentrepreneurs all operate in some degree or the other as financial agents in The Gambia. The privatization of the banking industry and the liberalization of financial markets have produced a much smaller, leaner, and more resilient financial sector wholly dominated by private commercial banks (Graham, et al., Chapter 1). While this was in many ways a necessary and inevitable result for sound banking in The Gambia, that change does little to supply financial services in the rural area.

By the year 1990, agricultural lending had declined substantially; the major rural bank had disappeared as an active lender; and agricultural parastatal linkages to the banking sector had been considerably reduced through reorganization and partial privatization. In the face of this growing lack of financial services in the rural sector, non-governmental organizations (NGOs) moved in to fill the gap and become the missing link to rural financial intermediation. Unfortunately, few NGOs were prepared to carry out any viable financial intermediation. Their approaches with diverse operating and financial technologies have only succeeded in creating negative externalities and distortions in rural financial markets (Graham, et al., Chapter 2). Amidst these failures, the village savings and credit

associations (VISACAs) have emerged as a much needed financial innovation in rural Gambia.

This paper reports on the findings for the VISACA movement as part of a research study of the financial markets in The Gambia carried out by the Rural Finance Program at the Ohio State University (Graham et al. 1992). The paper will specifically document the evolution and performance of the VISACAs in The Gambia. However, the rather unusual performance of the VISACAs has attracted donor attention and the paper will address a legitimate concern that outside donor could kill a perfectly healthy institution unless caution is exercised on what constitutes appropriate donor assistance.

II. A BRIEF HISTORY OF THE VISACAs IN THE GAMBIA

VISACAs (i.e. Village Savings and Credit Associations) have a primary objective of collecting local savings and making loans to individual villagers or groups. A total of six VISACAs function currently in villages in the Sapu region, about 350 kms East of Banjul, the capital of The Gambia. The VISACA pilot project was launched in 1988 with the Gambian Ministry of Agriculture and managed by Centre International de Développement et de Recherche (CIDR) a French NGO, in cooperation with Kreditanstalt für Wiederaufbau (KFW) of Germany and the government Jahally-Pacharr Rice Project.

Internal regulations of VISACAs are discussed and established at a general assembly of all villagers. Villagers decide upon membership conditions, interest rates for deposits and loans, and management procedures and practices. Each VISACA has a management committee among whose responsibilities are the evaluation and granting of loans. Each

management committee is composed of six to ten people, with an equal number of men and women. Two to three cashiers are also selected to carry out bookkeeping responsibilities. Accounting practices used in the VISACAs have been kept simple during this initial phase to facilitate cash flow management.

Membership fees have been sufficiently low (10 and 20 dalasis i.e $1 and $2) to attract the majority of villagers. Membership is required to make deposits and/or receive loans. Some VISACAs require their members to make a one-time deposit of any amount in order to become eligible for future loans.[1]

In general, VISACAs do not try to match the deposits of a particular person with his/her loan request as credit unions do with their loan multiple formulas. Instead they try to match the term structures of assets and liabilities of the VISACA as a whole. Loans are made out of three types of savings instruments, i.e. three, six, and nine month "term deposit" accounts. Twelve-month deposit accounts exist but have not received too much attention from VISACA members. Non interest bearing current account deposits (i.e. demand deposits) are also available but are not used for loan purposes, i.e. the VISACAs hold 100 percent reserves on demand deposits.

Four VISACAs set annual deposit rates at 20 percent and loan rates at 40 percent. Two VISACAs established 40 percent annual deposit rates and 60 percent annual loan rates. Thus, the annualized gross intermediation margin reaches 20 percent between deposit and loan rates. This margin compares to formal banks deposit rates of 10 to 12 percent and

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[1] It is interesting to note that CIDR did not ask the villagers to tie savings behavior to credit. However, on their own initiative most village VISACAs (4 out of 6) implemented the requirements of some prior savings before receiving a loan.

annual loan rates between 20 to 30 percent from 1988 to 1991. Furthermore, these high rates allow the VISACAs to more than compensate for inflation (around 10 percent over the past four years), generate interest earnings to cover incidental expenses, and create a growing surplus to service new loans.

III. VISACA SAVINGS AND CREDIT FLOWS

1. Savings Flows

A. Membership Participation and Savings Accumulation Through Time

Membership in the VISACAs consists of both individuals and kafo groups. Kafos are homogeneous groups of individuals in a village with common interests. Members of kafo groups can have individual accounts as well. The VISACAs as a whole recorded a growth in membership in 1991 roughly 2.8 times their 1988 membership for a total of 1305 villagers and kafo groups. Of this total there were 676 women (52%), 574 men (44%) and 55 (4%) kafo groups. Further findings show that by December 1991 up to 52 percent of the villagers were members in some VISACAs and, for all six villages, one-third of all villagers were VISACA members.

The VISACAs began collecting deposits in 1988. By December 1991, members with three, six and nine month savings accounts represented 47.4 percent of the total membership. Another 6 percent held demand deposits accounts. The most popular savings instrument among the membership is the six month term deposit. Twenty three percent of the membership held these accounts. Information from VISACA files indicate that by December 1991, a total of 399,693 dalasis had been mobilized cumulatively from their

inception by all six VISACAs in 698 demand deposits and savings accounts. At an average exchange rate of 1.00 dollar = 8 dalasis for the period, this amounts to a savings inflow of $49,961.6 dollars. Overall, VISACA members from all six villages have a relative preference for six month term deposits. These captured 33.8 percent of the accumulated deposit flow from 1988 until December 1991.

B. Growth of Deposit Outstanding Balances

Another revealing perspective is the trend in deposit growth for this three-year period of the VISACAs' life. As of December 1991, a total of 188,006 dalasis was outstanding in 485 accounts with an average balance of 388 dalasis per account. The growth was a little over three-fold for total outstanding deposits of all VISACAs for the two years from January 1st, 1989 through December 31st, 1991. Current account balances grew most rapidly (about 8 fold) followed by 6 month deposit balances (4 fold) and 3 months deposits balances (3 fold), with the longest term 9 month deposit instrument growing the slowest (2.4 times). As pointed out earlier in the cumulative data, the 6 month deposit account was uniformly the most popular savings instrument from 1989 to 1991, accounting in 1989 for 43 percent of total deposits, 58 percent in 1990 and 49 percent in 1991.

2. Loan Disbursement in the VISACAs

A. Credit Flows Through Time and Term Matching Practices

Lending is an important part of the VISACAs' operation and access to loans is valued highly. Despite what may appear as high interest rates (40 and 60 percent), the VISACA loan rates compare favorably to village money lender rates that can reach 140 percent per year. Since the VISACAs began disbursing loans in 1989, a total of 366,709

dalasis (45,838 dollars) have been issued cumulatively to 1266 members as of December 1991 resulting in an average loan size of 290 dalasis or about 36 U.S. dollars equivalent (see Table 1). The average loan term for all loans issued during this period has been 156 days (five months) which, not surprisingly, is approximately one month less than the preferred deposit term length. As a general policy, all VISACAs try to match the term structure of a given volume of loans with that of a comparable volume of deposits servicing those loans so as to be able to service anticipated deposit withdrawals or renewals. Thus, the proportion of people who receive a loan is very much dependent on membership through savings accounts.

B. Loan Practices and Characteristics of the Loan Portfolio

Loans are granted on a first-come, first-served basis according to available funds. VISACA loan committees make the final decision on loan approval and the amount approved. Collateral, often in the form of livestock or farm implements and gold jewelry for women, is required to secure a loan. Most loan applicants indicate trading as the purpose of their request although loans are issued for a wide variety of other purposes. The VISACAs do not engage in loan targeting.

In the year 1991 alone, 630 loans were granted to 48.3 percent of the total membership of the six VISACAs (see table 1.). According to a CIDR report in 1990, most loans went out for trade purposes as 56 to 97 percent of village specific VISACA loans were given out to shopkeepers, for petty trade, sale of coarse grain, and cattle trading (CIDR, 1990). The high share of loans for trading activity and fewer loans for farming was explained by the presence of other NGOs in the area that specialized in granting fertilizer

and farm equipment loans at very low interest rates. Given the relatively short term loans in the VISACAs (more commonly three to six months), most loans would not be expected to support agricultural production that has a longer seasonal gestation. Many loans are used to finance village trading activity in which the inventory turnover of goods is consistent with the shorter term structure and where trade margins can support higher interest rates than those commonly associated with agriculture.

C. The Philosophy of Term Matching Practices

The term matching feature so characteristic of VISACAs deserves more comment. Any financial institution must be prepared to engage in responsible liquidity or cash flow management. Loan repayments must be scheduled in such a way as to facilitate deposit withdrawals. Moreover, this must be programmed so that possible delays in repayments do not lead to a liquidity crunch (i.e. an inability to service regularly scheduled deposit withdrawals or renewals). The VISACAs protect themselves from this risk through two mechanisms: the high interest rate margins pointed out earlier and the staggered scheduling of loan terms for a period shorter than the deposit instrument supporting this lending. The twenty point margin between deposit and loan rates generates substantial net interest earnings to contribute to the funds needed to cover deposit withdrawals in the face of late loan repayments. At the same time, a given volume of three month deposits are drawn upon to support a comparable volume of loans but staggered or shortened to two months or less in term, six month deposits support loans at five month terms or less, etc. In this way, VISACAs are able to meet obligated term deposit withdrawals when they mature except in the case of extreme loan delinquency, a rare event in most VISACAs.

III. LOAN RECOVERY PERFORMANCE

Table 2. documents loan disbursement and loan recovery for the VISACAs for all 954 loans issued and due for repayment from January 1st 1989 through December 31st 1991. All due dates for repayment fell within this three year period. Five VISACAs had complete information on loan disbursements and loan recovery. Since Village 2 began operations only in 1991, none of its 29 loans issued in 1991 fell due during this year. One VISACA, Village 3, issued 50 loans during this two year period, however, the research team was unable to secure any information on the loan repayment status of these loans.

Based on the information on the four VISACAs that had a documented history of loan disbursements and loan recovery from January 1989 through December 31st 1991, the overall repayment rate was an outstanding 94.4 percent by number of loans and 94.7 percent by the volume of loans (Table 2, column 8). The best performing VISACAs were Village 6 and Village 1 with a remarkable 97 percent loan recovery rate over this three year period. The lowest repayment was recorded by Village 5 at 90 and 92 percent a still very fine performance. For the VISACAs as a whole, some delay in loan repayment (typically 30 days) is a very common phenomenon and this suggests that VISACAs may well be playing an interesting insurance role by allowing groundnut producers and traders, along with other borrowers, more flexible loan terms to repay their loans somewhat later than scheduled.

Table 3 highlights this issues in detail through documentation of the time profile of loan repayments for all 906 loans in the four VISACAs discussed above. Overall roughly 37 percent of all loans due were repaid promptly or in advance whereas 36 percent of the loans were repaid one month late, approximately 16 percent between one and three months

late, and 4.3 percent more than three months late (panel B, column 7). It is interesting to note that a significant part of all loans (30 percent) were repaid early.

In summary, the VISACAs, record outstanding repayment records over this three year period. No other formal financial intermediary or NGO in The Gambia can match this performance with the possible exception of the branches of two foreign commercial banks in Banjul but no data on loan recovery or arrears are publicly available for these private banks, hence comparisons are not possible. Furthermore, judged on the risks inherent in the VISACAs portfolio, i.e. an overwhelming low income rural constituency, the above performance stands out as an unusual achievement.

A final indicator of the remarkable performance of the VISACAs is its loan deposit ratio of 100 percent, i.e. the term matching practice of the VISACAs for loans and deposits, excluding demand deposits, means they operate with a one-to-one loan deposit ratio. This ratio is much higher than that characteristic of credit unions worldwide (50 to 60 percent) who hold much of their savings in deposit accounts in branches of banks rather than using them for loans. Similarly, this ratio is much higher than that of the private banks in The Gambia (33 percent) who allocate most of their deposit resources into treasury bills or other non-loan assets. This high ratio for the VISACAs implies a "no reserve" policy for time deposits, a seemingly risky practice. However, since 100 percent reserves are held on demand deposits this compensates for no reserves held on time deposits.

IV. THE EXTERNAL FUNDING ISSUE

The VISACAs were able to mobilize 304,098 dalasis from their savings accounts (excluding current accounts which are not used for loans) while, as pointed out above, 366,709 dalasis were issued cumulatively to members as loans (see Table 1). The shortfall in funding (62,611 dalasis) was obtained through external funds in June 1991. External donors lent 30,000 dalasis to the VISACAs' management at 11 percent annual interest for nine months. The management in turn lent to two VISACA villages at the same 11 percent interest rate for the same nine months maturity (without revealing the source of the funding). Each village then lent to its respective members at 40 and 60 percent annual interest rates for eight months. Borrowers thus paid an effective 27 percent and 40 percent interest on their eight months loans. For the first experiment with donor funds, the effective margin for VISACAs was 18.4 percent [(40% x 8/12)-(11% x 9/12)] and 31.75 percent [(60% x 8/12)-(11% x 9/12)] respectively.

Donors in conjunction with the CIDR plan to reward in the future all VISACAs that show impressive savings and loan recovery performances. The gradual introduction of some outside funding could possibly allow these associations to expand their loan activities and engage in some term transformation (i.e. make longer term loans) as long as the relative share of outside money remains a distinctly minor share of total funding and is not associated with any earmarked or targeted loan scheme. Currently outside money has reached almost 10 percent (9.86 percent) of total funding and 14.7 percent of 1991 savings. Fortunately, all these loans were repaid by March 1992, indicating that the experiment worked successfully this one time. Nevertheless, it might be risky to increase this outside

funding much beyond the 20 percent range without placing at risk the VISACAs' incentive structure for repayment and saturating the market for secure lending opportunities in these villages.

One important lesson of program design in the VISACA experience is to appreciate the logic of a two stage sequence of donor involvement in promoting local savings and credit associations. In the first stage, donor support was focused on promotion, technical assistance, and training, with a long term resident advisor working closely with the VISACAs. No external funding was provided for on-lending. The objective was to promote properly remunerated local savings deposits as the exclusive base for on-lending, thereby ensuring local identity and local control and autonomy in decision making, both of which are essential ingredients for promoting responsible loan recovery.

The second stage, some three to four years later, allowed for some donor funding to be used for on-lending through the vehicle of 9 month or 1 year deposits. This expands the base for on-lending beyond the limits set by the local deposit base. It also allowed longer term loans that could support agricultural activities. However, there is little likelihood that these longer term loans would move substantially into agriculture if borrowers have to pay 40 to 60 percent annualized interest charges (depending on the VISACA). It is unlikely that any agricultural activity earns that kind of return in The Gambia. To ensure the continued success of donor funding, the loan activity that grows out of this action needs to remain untargeted, to therefore blend into the generalized practices used for other loans. An important caveat to this second stage of donor intervention is thus, to limit the volume of outside funding for on-lending to no more than 15 to 20 percent of total lending sources.

Otherwise, the image of local identity, local control and, most importantly, local savings could become jeopardized as a donor virus could contaminate the portfolio with an entitlement or dole psychology, and borrowers "take the money and run."

VI. LESSONS LEARNED AND CONCLUDING REMARKS

The single most important feature behind the VISACAs success is the local savings mobilization dimension that has nurtured and expanded the funding base from its inception in 1988 to the present. This feature quickly established the legitimacy of these young associations. It meant that villagers controlled their own association, guaranteed their autonomy in decision making and introduced a moral authority for responsible loan administration and loan recovery of their own funds. This locally mobilized resource base clearly created the environment for local village assemblies to meet and discuss such questions as the composition and responsibilities of the management committees and the establishment of interest rate policies and composition of savings instruments.

The next stage of the VISACA movement is the most challenging, namely, expanding the movement into a larger number of villages in several other regions of the country. This action could begin to create a network of VISACAs that, in effect, would generate scale, scope and spatial economies and possible linkages to the banking system. That is one area where donor money could be effectively used. This would occur only if a second level regional federation would emerge that could play a role in intermediating between surplus and deficit units within the movement, become a lender of last resort, and a service center for auditing and other technical assistance. It may be premature to expect this to emerge

in the immediate future. However, it is not an unreasonable long term objective as long as there are other regions in The Gambia that can generate the income streams for savings mobilization comparable to those generated by the Jahally-Pacharr project.

The contrasting operational philosophies between the VISACAs, on the one hand, and other NGO operators in The Gambia, on the other hand, has undoubtedly led to the great success enjoyed by the VISACA movement today. The VISACAs are the only entity in The Gambia that has created a viable, village based savings and credit movement. It would be wise if the donor community would contain this urgent need to "pour" money to an operation that has proven that sound money management goes hand in hand with local people's money and limited outside resources.

Table 1 **Savings Accumulation (in Dalasis) vs. Loan Disbursement Through Time in the VISACAs from 1988 to December 1991.**

	Savings[1]	Loans	
Year	Amount	Number	Amount
1988	5780	0	0
1989	41,133	209	38,445
1990	128,790	427	124,615
1991	128,395	630	203,649
TOTAL	304,098	1266	366,709

Note 1: Savings does not include demand deposits
Source: VISACA Files.

Table 2 **Documentation of Loan Recovery by Number of Loans and by Volume of Loans by VISACA for all Loans Issued from 1989 Onwards and Due for Repayment through December 1991.**

	Total Loans Issued as of December 1991		Total Loans Issued and Due by December 1991		Loans Due and Repaid by December 1991		Recovery Rate for Loans in %	
VISACA	No.	Amount	No.	Amount	No.	Amount	No.	Balances
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Village 1	120	44,526	72	37,470	70	36,340	97.2	97.0
Village 2	29	2,760	0	0	0	0	-	-
Village 3[1]	50	13,100	48	13,035	-	-	-	-
Village 4	406	101,113	324	72,398	307	67,388	94.8	93.1
Village 5	387	109,350	250	72,775	226	66,975	90.4	92.0
Village 6	274	95,860	260	88,295	252	85,945	96.9	97.3
Total	1,266	366,709	954	283,973	855	256,648	94.4	94.7

Source: VISACA files.
Note 1: No information was available on Village 3 loan repayment.

Table 3 Basic Documentation of Time Profile of Loan Repayments in Terms of Number of Loans and Rates of Repayment for Total Number of Loans Issued and Due for Repayment from January 1st 1989 Through December 31st 1991 by VISACA.

A. Number of Loans							
Indicator/Schedule	Village 1	Village 2	Village 3	Village 4	Village 5	Village 6	Total
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
1. Loans due	72	0	-	324	250	260	906
2. Repaid on time	21	-	-	18	8	17	64
3. Repaid ahead of time	19	-	-	87	102	65	273
4. Repaid but less than a month late	25	-	-	132	67	103	327
5. Repaid but 1 to 3 months late	5	-	-	61	30	46	142
6. Repaid but more than 3 months late	0	-	-	9	10	20	39
7. Undetermined length[1]	0	-	-	0	9	1	10
B. Rates of Loan Repayment by Time Profile of Repayments							
1. Prompt recovery rate (%)[2]	29.2	-	-	5.6	3.2	6.5	7.1
2. Early recovery rate (%)[3]	26.4	-	-	26.9	40.8	25.0	30.1
3. Less than a month arrears rate (%)[4]	34.7	-	-	40.7	26.8	39.6	36.1
4. One to 3 months arrears rate (%)[4]	6.9	-	-	18.8	12.0	17.7	15.7
5. More than 3 months arrears rate (%)[4]	0.0	-	-	2.8	4.0	7.7	4.3
6. Undetermined length recovery rate	0.0	-	-	0.0	3.6	0.4	1.1
7. Total recovery rate (%)[5]	97.2			94.8	90.4	96.6	94.4

Note 1: Undetermined length refers to loans with no due date listed in VISACA files..

2: Prompt recovery rate was obtained by dividing the number of loans repaid on time in line 2, panel A, by the number of loans due in line 1, panel A.

3: Early recovery rate was obtained by dividing the number of loans repaid ahead of time (line 3, panel A) by the total loans due (line 1, panel A).

4: Recovery rates for less than one month in arrears, from one to three months in arrears, etc. is based on the number of loans finally repaid during these specified periods (lines 4, 5, and 6 in panel A) over the number of loans due (line 1).

5: Total recovery rate (line 7, panel B) is derived by adding up all the recovery rates estimated in lines 1-6, panel B.

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